SECTION 22000 PROGRAM AREA HIRING CREDIT

References (Repealed Sections) 17053.11; 23623

Program Areas converted to Enterprise Zones as of January 1, 1997. Prior to this date, taxpayers had to be certified by the California Trade and Commerce Agency or TCA in order to be eligible to utilize the Program Area tax incentives. TCA could certify a taxpayer to take the hiring credit only or all five Program Area incentives. The type of certification is determined from the certification letter.

Certification was generally valid for three years. After three years, the taxpayer would have to be re-certified. De-certification could occur if a company failed to meet the requirements.

The Program Area hiring credit applies to those employees hired after the designation date of the Program Area. No credit is allowed for employees hired after the Program Area designation expires. However, for income and taxable years beginning on or after January 1, 1997, Program Areas were converted to Enterprise Zones (EZs) and are entitled to the benefits available to EZs (see EDAM 2000 - 7000).

The following Program Area discussion relates to income and taxable years beginning prior to January 1, 1997.

22100 Geographic Boundaries and Designation Dates

For a listing of Program Area cities, see "Program Area Locations and Designation Dates " EDAM 1360. To verify an address, refer to EDAM 1300.

22200 Qualified Business

References (Repealed Sections) 17053.11(b)(1); 23623(b)(1)

EDAM 22210 Change in the Form of the Trade or Business

A "qualified business" *eligible for all five* of the Program Area tax incentives, is a business certified during the income or taxable year as meeting one of the following standards based on its *total work force* in the Program Area:

- 50% of its Program Area work force are residents of a high density unemployment area (HDUA); or
- 30% of its Program Area work force are residents of a HDUA and the company must contribute to an approved community service program;

The business may also qualify if persons owning at least 30% of the business are residents of a HDUA.

A "qualified business" *eligible for the hiring credit only*, is a business certified during the income or taxable year as meeting one of the following standards *based ONLY on those employees hired by the business in the Program Area within the 12 months period immediately preceding the date certification is sought*:

- 50% of its Program Area work force are residents of a high density unemployment area (HDUA); or
- 30% of its Program Area work force are residents of a HDUA and the company must contribute to an approved community service program;

The business may also qualify if persons owning at least 30% of the business are residents of a HDUA.

22210 Change in the Form of the Trade or Business

References (Repealed Sections) 17053.11(f)(2)(F); 23623(f)(2)(F)

The employment relationship between the taxpayer and an employee is not treated as terminated by reason of a mere change in the form of conducting the trade or business. If the employee continues employment in that trade or business and the taxpayer retains a substantial interest in that trade or business, the employee is not treated as terminated.

22300 Qualified Wages

References (Repealed Sections) 17053.11(e); 23623(e)

EDAM 22310 Estates and Trust
EDAM 22320 Minimum Wage Chart

Qualified wages are wages paid or incurred to employees (qualified) during the consecutive 60-month period beginning with the first day the employee commences employment with the taxpayer.

In general, *qualified wages* means that portion of hourly wages that does not exceed 150% of the minimum wage.

- Minimum wage means the wage established by the Industrial Welfare Commission. When the California minimum wage is higher than federal minimum wage, use the California minimum wage for purposes of this credit.
- To determine a salaried employee's hourly wage, divide the total salary by the average hours worked, normally 2,000 hours per year.

22310 Estates and Trust

In the case of an estate or trust, the qualified wages are apportioned between the estate/trust and the beneficiaries on the basis of the income allocable to each. Consequently, any beneficiary, to whom wages are apportioned, is treated as the employer with respect to those wages.

22320 Minimum Wage Chart

EFFECTIVE DATE	MINIMUM WAGE	MAXIMUM HOURLY WAGE - HIRING CREDIT
July 1, 1988 to September 30, 1996	$4.25	$6.37 (150% of $4.25)
October 1, 1996 to February 28, 1997	$4.75	$7.12 (150% of $4.75)
March 1, 1997 to August 31, 1997	$5.00	$7.50 (150% of $5.00)
September 1, 1997 to February 28, 1998	$5.15	$7.72 (150% of $5.15)

22400 Qualified Employee

References (Repealed Sections) 17053.11(b)(2); 17053.11(c); 17053.11(d); 23623(b)(2); 23623(c); 23623(d)

EDAM 22410 Leased Employees

A *qualified employee* is an individual who was an unemployed resident of a HDUA, for three or more months prior to employment with the qualified business. Participation by a prospective employee in a state or federally funded job training or work demonstration program does not constitute employment, or affect the eligibility of an otherwise qualified employee.

A *qualified employee* also includes an otherwise qualified individual who is employed by a qualified business in the 90 days prior to the business' certification by the TCA.

22410 Leased Employees

The "employer" is the qualified taxpayer and may qualify for the hiring credit for leased employees. The employer can be either the leasing company or the subscriber to the leasing company. Generally, the employer can be identified due to the legal obligation to pay the payroll taxes of the employee, and as to who has the right to control and direct the workers (employee's) services.

Internal Revenue Service (IRS) Publication 15-A, *Employer's Supplemental Tax Guide* provides guidelines for establishing an employment relationship and provides examples to consider in determining the employer-employee relationship.

22500 Credit Computation

References (Repealed Sections) 17053.11(a); 17053.11(c) & (d); 23623(a); 23623(c) & (d)

EDAM 22510	Reduction for Other Tax Credits
EDAM 22520	Wage Expense Deduction
EDAM 22530	Business Income Activity Limitation
EDAM 22540	General Provisions – Apportionment of Business Income
EDAM 22541	Property Factor – Income Apportionment
EDAM 22542	Payroll Factor – Income Apportionment
EDAM 22543	Sales Factor – Income Apportionment
EDAM 22544	Apportionment – Combined Groups
EDAM 22545	Apportioning for Personal Income Tax Taxpayers
EDAM 22550	S Corporations

For each income or taxable year a hiring credit is allowed to a qualified business for hiring a qualified employee who was unemployed for *at least six (6) months*. The credit is equal to the sum of each of the following:

- 50% of the qualified wages during the first year of employment.
- 40% of the qualified wages during the second year of employment.
- 30% of the qualified wages during the third year of employment.
- 20% of the qualified wages during the fourth year of employment.
- 10% of the qualified wages during the fifth year of employment.

For those qualified employees unemployed for at least three (3) months but less than six (6) months, the credit is equal to the sum of the following:

- 25% of the qualified wages during the first year of employment.
- 40% of the qualified wages during the second year of employment.
- 30% of the qualified wages during the third year of employment.
- 20% of the qualified wages during the fourth year of employment.
- 10% of the qualified wages during the fifth year of employment.

The credit percentage is based on the employee's date of employment and subsequent anniversary dates. The taxpayer's tax year does not control the applicable credit percentages. With the exception of the first and last year of the credit, within one tax year, two percentage ranges for the computation of the credit may apply.

Example: An employee was hired 7/1/1995, and the taxpayer is completing the tax return for the year ending 12/31/1996. For the period 1/1/1996 to 6/30/1996, the hiring credit is based on 50% of qualified wages. For the period 7/1/1996 to 12/31/1996, the hiring credit is based on 40% of qualified wages.

Once the employee commences employment, the credit percentage range begins and generally is not interrupted in the event of a subsequent layoff and rehire of the employee.

Example: An employee is hired 7/1/1995, is temporarily laid off 2/1/1996, and is rehired 4/1/1996. The 50% credit range runs from 7/1/1995 to 6/30/1996 regardless of the layoff period between 2/1/1996 and 3/31/1996.

22510 Reduction for Other Tax Credits

References (Repealed Sections) 17053.11(h); 23623(g)

The Program Area hiring credit is reduced by the credit allowed under California Revenue & Taxation Code Section (CR&TC §) 17053.7 & 23621 (Jobs Tax Credit), and the federal credit allowed under IRC §51 (Work Opportunity Tax Credit – WOTC).

22520 Wage Expense Deduction

References (Repealed Sections) 17053.11(h); 23623(g)

The taxpayer must reduce any deduction for wages by the amount of the Program Area hiring credit allowed (including any current year credit carried forward).

22530 Business Income Activity Limitation

References (Repealed Sections) 17053.11(j); 23623(i)

The amount of hiring credit or sales or use tax credit (see EDAM 23000) claimed, including any credit carryover from prior years, may not exceed the amount of tax on the taxpayer's Program Area business income in any year. The Program Area business income is that portion of *worldwide* business income that is apportioned to the Program Area. Non-business income or loss is not included in the calculation of business income from the Program Area. Each taxpayer claiming the credit must compute the Program Area business income and resulting tax.

Example: Corp. A operates entirely within a Program Area. In order to determine the amount of hiring credit allowable, the business income and the tax on that business income must be determined. Corp. A has the following items of income and expense:

Income from business operations	$30,000
Interest from investment which is unrelated to Corp. A's business operations	2,000
Business expenses	(17,000)
Net taxable income before taxes	$15,000

Corp. A's income attributed to business operations is:

Income from business operations	$30,000
Business expenses	(17,000)
Net Business Income	$13,000

To determine the Program Area hiring credit allowable, the net business income is multiplied by the current tax rate.

Net Business Income	$13,000
x 9.3%	.093
Tax associated with business income	$1,209

In this example, the taxpayer can offset the tax of $1,209 with the hiring credit available (up to $1,209).

NOTE: "net tax"/"tax" and alternative minimum tax impose limitations on the allowable offset but were not considered a factor in this example.

22540 General Provisions – Apportionment of Business Income

References (Repealed Sections) 17053.11(j)(2); 23623(i)(2)

If a business is located within and outside of a Program Area, or in more than one Program Area, the taxpayer must determine the portion of the total business income that is attributable to each Program Area.

- Business income is defined under the provisions of the Uniform Division of Income for Tax Purposes Act (UDITPA).
- Components of the factors are defined under the provisions of UDITPA.

For income or taxable years beginning on or after January 1, 1991, and ending on or before December 31, 1996 (1991 - 1995 years and 1996 calendar year taxpayers), business income is apportioned to the Program Area by multiplying the *worldwide* business income by a fraction, the numerator of which is the property factor plus the payroll factor, and the denominator of which is two (2).

For 1996 fiscal years, income or loss attributed to the Program Area is determined by multiplying *worldwide* business income or loss by a fraction, the numerator of which is the property factor, payroll factor, and sales factor (double weighted), the denominator of which is four (4).

For income or taxable years beginning before January 1, 1991, income or loss attributed to the Program Area is determined by multiplying *worldwide* business income or loss by a fraction, the numerator of which is the property factor, payroll factor, and sales factor, the denominator of which is three (3).

22541 Property Factor – Income Apportionment

References (Repealed Sections) 17052.13(f) 23612(f)

The property factor is a fraction. The numerator of the property factor is the average value of the real and tangible personal property owned or rented and used or available for use by the taxpayer *within the Program Area* during the income or taxable year. The denominator is the average value of all real and tangible personal property owned or rented and used or available for use during the income or taxable year *worldwide*.

Rented property is valued at eight (8) times the net annual rental rate. The net annual rental rate is the total rent paid for the property, less any subrental rates paid by subtenants.

22542 Payroll Factor – Income Apportionment

References (Repealed Sections) 17052.13(f) 23612(f)

The payroll factor is a fraction. The numerator of the payroll factor is the total compensation paid to employees working for the taxpayer *within the Program Area* during the income or taxable year. The denominator is the total compensation paid to employees working *worldwide* during the income or taxable year.

22543 Sales Factor – Income Apportionment

The sales factor is a fraction. The numerator of the sales factor is composed of the gross receipts as defined under the provisions of CR&TC §25134 - 25136, derived during the taxable or income year from transactions and activities occurring within the taxpayers trade or business in the Program Area. The denominator is composed of the gross receipts as defined under the provisions of CR&TC §25134 - 25136, derived during the taxable or income year from transactions and activities related to worldwide operations

General rules regarding the double weighting of the sales factor are applicable.

Example: For the income year ending 12/31/95, Corporation A operates within and outside a Program Area. Total business income of $13,000 needs to be apportioned to the Program Area. The following amounts apply to Corp. A's property and payroll:

Program Area Property	$40,000
WW Property	$100,000
Program Area Payroll	$5,000
WW Payroll	$10,000

Program Area Property/WW Property	=.40	
Program Area Payroll/WW Payroll	=.50	
	.90/2 = .45	Program Area Apportionment Factor

Business income	$13,000
Apportionment Factor	x 0.45
Program Area Business Income	$5,850
Current Tax Rate (Prior to 1997 – 9.3%)	x 0.093
Tax attributable to Program Area business income	$544

22544 Apportionment – Combined Groups

For members of a combined group, the credit limitation will be based on the combined groups worldwide business income (before CA apportionment). The numerator of the apportionment formula will be based on each Program Area taxpayer's separate Program Area payroll and property amounts (and sales as discussed in EDAM 22543) and the denominator will be based on the combined groups worldwide payroll and property amounts (and sales as discussed in EDAM 22534).

Example: For the income year ending 12/31/95, Parent Corporation A has two subsidiaries, B and C. Corporations A and B operate within a Program Area. The combined group operates within and outside California and apportions its income to California using Schedule R. The combined group's business income is $1,000,000.

Business income apportioned to the Program Area was determined as follows:

	A	**B**	**C**	**Combined**
<u>Property Factor</u>				
Program Area Property	$2,000,000	$1,000,000	$0	$3,000,000
Worldwide Property				$5,000,000
Apportionment %	40%	20%		60%
<u>Payroll Factor</u>				
Program Area Payroll	$2,000,000	$800,000	$0	$2,800,000
Worldwide Payroll				$4,000,000
Apportionment %	50%	20%		70%
Average Apport. % (Property + Payroll Factors)/2	45%	20%		65%
Business Income				$1,000,000
Program Area Income	$450,000	$200,000		$650,000

22545 Apportioning for Personal Income Tax Taxpayers

The following examples show the application of the apportioning rules to personal income tax taxpayers.

Example: Ray Smith is vice president of an S corporation that has two locations, one within a Program Area and one outside the Program Area. Eighty percent (80%) of the S corporation's business is attributable to the Program Area. (**NOTE**: This percentage was determined by the S corporation, using Worksheet V from the FTB 3805Z Business Booklet, at the time the S corporation return was prepared). Ray divides his time equally (50% & 50%) between the two offices of the S corporation.

Mary Smith (Ray's spouse) works for the S corporation at its office located within the Program Area.

Ray and Mary Smith have the following 1996 items of California income and expense:

Ray's salary from the S corp.	$100,000
Mary's salary from the S corp.	75,000
Interest on savings account	1,000
Dividends	3,000
Schedule K-1(100S) from the S corp.	
Ordinary income	40,000
Program Area business expense deduction	(5,000)*
Ray's unreimbursed employee expenses from Schedule A	(2,000)

*The Program Area business expense deduction is a separately stated item on Schedule K-1 (100S).

The Smith's Program Area income is computed as follows:

Ray's Program Area salary ($100,000 x 50%)	$50,000
Mary's Program Area salary ($75,000 x 100%)	75,000
Pass-through ordinary income from the S-Corp. ($40,000 x 80%)	32,000
Program Area business expense deduction from the S-Corp.	(5,000)
Ray's unreimbursed employee business expenses (2,000 x 50%)	(1,000)
Total Program Area income	$151,000

Ray and Mary must compute the tax on the total Program Area income of $151,000 (as if it represents all of their income). Using the tax rate schedule for the filing status *married filing joint*; the 1996 tax on $151,000 is $10,938. The $10,938 is the first limitation on Program Area credits for the 1996 tax year. The second limitation on the credits is the *net tax* on all income.

NOTE: The standard deduction and personal or dependency exemptions are not included in the computation of Program Area income since they are not related to trade or business activities.

22550 S Corporations

References 23803(a)(1)(A); 23803(a)(1)(F)

An S corporation's hiring credit may reduce the Program Area tax at both the corporate and shareholder levels. However, the S corporation may only use one-third (1/3) of the credit to reduce the tax on the S corporation's Program Area income.

One hundred percent (100%) of the Program Area credit is passed through to the S corporation shareholders. The full amount of the credit is reported on Schedule K (100S) and passed through to the shareholders on Schedules K-1 (100S).

The wage reduction for the S corporation is equivalent to the 1/3 credit amount. The wage reduction for the shareholders is 100% of the credit amount, equal to the amount of credit passing through to them.

Example: An S Corporation computes a $3,000 hiring credit. The S corporation's credit is $1,000 and the wage reduction is $1,000. The $3,000 credit is passed through to the S corporation's shareholders, and the wage reduction recognized by the shareholders is $3,000.

22600 Credit Usage & Carryover

References (Repealed Sections) 17053.11(i); 17053.11(j)(1); 17053.11(j)(3); 23623(h); 23623(i)(1); 23623(i)(3)

The total amount of Program Area hiring and sales or use tax credits, including any credit carryover from prior years, that may reduce the "net tax"/"tax" for the income or taxable year, shall not exceed the amount of tax imposed on the taxpayer's business income attributable to the Program Area, determined as if that income represented all of the income of the taxpayer.

The portion of the credit that exceeds the "net tax"/"tax" for the income or taxable year, is carried over and added to the credit, if any, in the following year. The credit is carried over to succeeding years, until it is exhausted.

Example: A taxpayer has a $4,900 Program Area hiring credit. Tax imposed on Program Area business income is $4,700 and the taxpayer's overall "net tax"/"tax" is $4,000. The taxpayer would be eligible to claim a $4,000 maximum hiring credit.

Total hiring credit	$4,900
Tax on Program Area income	$4,700
First limitation:	
Lesser of total credit or tax on Program Area income	$4,700
Second limitation:	
Lesser of tax on Program Area income or "*net tax*"/"*tax*"	$4,000
Maximum credit allowed:	
Lesser of *Program Area tax limitation* or "*net tax*"/"*tax*" *limitation*	$4,000
Total hiring credit	$4,900
Maximum credit allowed	$4,000
Carryover	$ 900

22610 Credit Will Not Reduce Certain Taxes

The Program Area hiring credit cannot reduce the:

- Minimum franchise tax (corporations, limited partnerships, limited liability partnerships, LLCs, and S corporations);
- Built-in gains tax (S corporations);
- Excess net passive income tax (S corporation);
- Alternative minimum tax (corporations, exempt organizations, individuals and fiduciaries); or
- Regular tax below tentative minimum tax (TMT) before January 1, 1993

NOTE: For income or taxable years beginning on or after January 1, 1993, the Program Area hiring credit may reduce regular tax below TMT.

22620 Credit Recapture

References (Repealed Sections) 17053.11(f)(1); 17053.11(f)(3); 23623(f)(1); 23623(f)(3)

Recapture of the hiring credit is required if the employee is terminated before the end of the longer of the following two periods:

- The first 270 days of employment (whether or not consecutive); or
- Ninety (90) days of employment plus 270 calendar days,

A ‘‘day of employment’’ includes any day the employee was paid to work, regardless of whether the employee actually worked (including paid holidays, sick days, and vacation days).

To recapture the credit, the taxpayer must add to the current year's tax the amount of credit claimed for the year of termination, as well as all prior year credit claimed for the terminated employee.

NOTE: Any increase in tax, due to credit recapture, cannot be offset by the current year hiring credit.

22621 Credit Recapture – Exceptions

References (Repealed Sections) 17053.11(f)(2); 23623(f)(2)

Credit recapture will not apply if the termination was:

- Voluntary on the part of the employee;
- Caused by the employee becoming disabled;
- Due to employee misconduct;
- Due to a substantial reduction in business; or
- In order to enable other qualified employees to be hired, creating an increase in the number of qualified employees and the hours of employment.

22700 Record Keeping Requirements

For each qualified employee, documentation should be kept to show the following:

- Employee name
- Date employee was hired
- Number of hours the employee worked for each month of employment
- Wage rate paid for each month of employment
- Schedule calculating the hiring credit
- Overtime hours
- Location where services were performed
- Date employee was terminated, and reason why